## UNITED STATES TAX COURT WASHINGTON, DC 20217

ERIK D. STARK,		)
	Petitioner(s),	) )
	v.	) ) Docket No. 14842-12 L.
COMMISSIONER	OF INTERNAL REVENUE,	)
	Respondent	) )
		) )
		) )
		)

## <u>ORDER</u>

This case was on the Court's May 20, 2013 trial calendar for Buffalo, New York. The Commissioner moved for summary judgment based on the administrative record, and petitioner Erik Stark filed his own cross-motion for summary judgment. The dispute arises from Stark's failure to properly withhold payroll taxes and the Commissioner's imposing the trust-fund-recovery penalty as a result. The Commissioner sought a levy to collect the amount, and Stark challenged it in a collection due process (CDP) hearing, claiming he could not afford to pay the penalty and requesting currently not collectible status. We must decide whether the Commissioner abused his discretion by sustaining the levy.

## **Background**

From 2000 to 2010, Stark owned and operated Aero Autocare, Inc. (Aero), a car repair business in Rochester, New York. Aero fell behind its quarterly payroll tax payments, and so the Commissioner imposed the trust fund recovery penalty for the unpaid amounts.<sup>1</sup> In May 2008, the Commissioner assessed the penalty for

<sup>&</sup>lt;sup>1</sup> Employers generally have to withhold payroll taxes from their employees' paychecks and hold these funds in trust for the United States. This is called the "trust fund" system. If the employer doesn't pay over the withheld money, the Commissioner can collect it from a "responsible"

tax periods ending 9/2004, 12/2004, 3/2005, 6/2005, 9/2005, 6/2006, and 9/2006. The total amount of penalties was \$70,631.57, of which \$67,917.35 remains unpaid.

In September 2011, the Commissioner sent Stark a notice of intent to levy regarding the unpaid trust-fund penalties, and Stark timely asked for a CDP hearing. Stark sent in a completed Form 433-A -- the form the IRS asks taxpayers to use to summarize their financial condition -- to the settlement officer before their meeting the next year. Stark's lawyer told the settlement officer that his client couldn't afford to pay.

Stark's 433-A showed a monthly gross income of \$2,034 and monthly expenses of \$3,899. After reviewing Stark's Form 433-A and accompanying documentation, the settlement officer made an initial determination that Stark's monthly gross income was actually \$3,474 and his monthly expenses were actually \$3,232, which would allow for monthly tax payments of \$242.

After a few more exchanges, the settlement officer made a final offer to let Stark pay \$240 a month for 24 months and then \$1,170 for the remainder of the allowable collection period -- the reason for the increase was some substantiated expenses that were set to end after 24 months. Stark rejected this offer, and wanted "currently not collectible" (CNC) status for anything more than \$100 a month. The settlement officer rejected this final counteroffer and issued the notice of determination sustaining the levy. Stark then petitioned this Court, claiming that the Commissioner abused his discretion by incorrectly overestimating his monthly income.

Stark does not challenge his underlying tax liability, and so our standard of review is abuse of discretion. *Sego v. Commissioner*, 114 T.C. 604, 610 (2000); *Goza v. Commissioner*, 114 T.C. 176, 181-82 (2000). This means that we look to see if the Commissioner's decision was based on an error of law or rested on a clearly erroneous finding of fact, or whether he ruled irrationally. *Antioco v. Commissioner*, 105 T.C.M. (CCH) 1234, 1237 (2013).

person," i.e., an actual person. who was required to pay over the tax. Money collected this way is called a trust-fund-recovery-penalty. *See Kovacevich v. Commissioner*, 98 T.C.M. 1, 1-2 (2009).

## **Discussion**

We may grant summary judgment when there is no genuine dispute of material fact and a party is entitled to judgment as a matter of law. Rule 121(b); *Sundstrand Corp. v. Commissioner*, 98 T.C. 518, 520 (1992), *aff'd*, 17 F.3d 965 (7th Cir. 1994). There is no genuine dispute of material fact here because both parties accept the documents Stark submitted with his Form 433-A. They differ only in their analyses of that information, and both have moved for summary judgment.

There are a number of reasons an account may be "currently not collectible" -- a taxpayer can't be located, an entity has liquidated, an assessment period has expired. Given Stark's submission of Form 433-A and his arguments about his inability to pay based on his income and expenses, he is likely arguing for CNC status based on hardship. A hardship exists if a taxpayer is unable to pay reasonable basic living expenses. IRM pt. 5.16.1.2.9(1) (May 5, 2009).<sup>2</sup> This determination is based on a taxpayer's equity in assets, gross income, and necessary expenses. *Id.* Having CNC status doesn't mean a taxpayer's liability is absolved, but it does stop collection action by the Commissioner for a time.

Stark's Form 433-A showed essentially no equity in assets, monthly gross income of \$2,034, and monthly expenses of \$3,899. If these numbers are true, a levy on Stark's property would create a hardship under the Commissioner's own guidelines. After examination, however, the Commissioner increased Stark's monthly gross income and decreased his expenses, which showed Stark did have some extra income that he could use to pay part of his tax debt.

Stark disagrees with the Commissioner's adjustments, and we'll address each of his arguments in turn. To determine a taxpayer's ability to pay, the Commissioner should follow the procedures outlined in part 5.15.1 of the IRM. See IRM pt. 5.16.1.2.9(1) (May 5, 2009). The IRM instructs IRS officers to divide a taxpayer's annual income by twelve to determine monthly income if the taxpayer's income is sporadic. IRM pt. 5.15.1.11(2) (May 9, 2008). At the time of his CDP proceedings, Stark worked for Summit View Auto, where he at one point was paid both a base salary and commission. Stark arrived at his future monthly

<sup>&</sup>lt;sup>2</sup> We refer to the version of the internal revenue manual (IRM) in effect at the time of the CDP hearing.

income of \$2,034 based on a projection from a few more recent pay stubs. He claims this lower amount better reflected current business.

A review of Stark's pay stubs reveals the flaw in his analysis. Looking just at his pay stubs from September through December, Stark earned commissions, in order, of \$600, \$700, \$500, \$950, \$200, \$0, and \$950. And while the first two pay stubs of December didn't show any earned commission, the pay stub after showed \$500 and the one just before showed \$850. Two bad weeks in a row in December do not qualify as a trend demonstrating reduced future income. These pay stubs reveal a sporadic income week to week, and so the Commissioner was justified in averaging Stark's weekly commissions over the prior year. The Commissioner ignored Stark's past base salary of \$500 a week because he was no longer earning it, but looking just at commission income listed on 51 pay checks through 2011 led to a total of \$40,890, and a monthly income of \$3,474. That is what the IRM directs him to do in this situation, and is entirely reasonable. No abuse of discretion here.

The parties also disagree about Stark's monthly expenses. When determining CNC status, a taxpayer is allowed to include expenses that are necessary for his and his family's health, welfare, and production of income; and for certain expenses such as housing and health care. The IRS has published national and local standards of allowable amounts for its agents to use as guidelines for what is reasonable -- a taxpayer may exceed them, but only with adequate justification and substantiation. IRM pt. 5.15.1.7 (Oct. 2, 2009). Stark claimed monthly expenses of \$3,899. The Commissioner allowed some in their entirety -- such as food and clothing and housing -- and adjusted others. We won't review all of them, but some of the adjustments included reducing Stark's vehicle operating expense, his health insurance and out-of-pocket health-cost expenses, and disallowing \$497 a month in "other secured debt," which Stark later explained were legal fees related to his tax issues. The Commissioner initially allowed \$3,232 in expenses, which when combined with Stark's income of \$3,474, resulted in over \$242 of extra money a month.

We see no abuse of discretion in his adjustments to Stark's car and health-care expenses. The lower health-insurance cost was a result of the Commissioner's averaging costs over the year rather than looking at just the last pay stub, which was a reasonable decision. Stark's out-of-pocket health-care cost was the prorated amount of three pairs of glasses and dental costs he'd *already paid*. The expenses used to determine CNC are supposed to be future expenses that would affect Stark's ability to pay going forward. It was reasonable for the Commissioner to

lower this amount. The settlement officer also reduced Stark's car-operating costs to the maximum amount allowed and eliminated Stark's \$430 ownership expense after two years. She made a reasonable estimate of how long it would take to pay off the balance on Stark's car given its value and payment amounts. Stark argued that when done paying off his car he'd immediately get a new one, but this is too speculative.

Stark has two more arguments. First, he claims that when the Commissioner increased his gross monthly income, his \$380 tax expense also should have increased. This is a fair argument. Stark estimated his \$380 monthly tax expense based on weekly gross income of \$473, which corresponds to his claimed monthly gross income of \$2,034. After receiving Stark's Form 433-A, the settlement officer said she was "allowing the \$380 in taxes." The settlement officer also increased Stark's gross monthly income from \$2,034 to \$3,474. Common sense would suggest that a monthly increase in income of \$1,400 would also result in an increase in monthly taxes. And the IRM not only suggests, but directs the Commissioner to make an adjustment. See IRM pt. 5.8.5.20.4(10) (Oct. 22, 2010) ("If an adjustment to the taxpayer's income is made, an adjustment of the tax liability must also be made. Current taxes include federal, state, and local taxes.")<sup>3</sup> The IRM of course is not binding law, but we think the Commissioner's failure to make this adjustment calls his determination into question. We do not know necessarily whether \$380 is the correct monthly tax expense for Stark, but after accepting the amount when provided alongside an income of only \$2,034, the Commissioner should've either increased it or at least explained why he was still using it. But there is no such explanation. This is irrational, and it makes review of the Commissioner's determination difficult. Quality Software Sys. Inc. v. Commissioner, 109 T.C.M. (CCH) 1550, 1555 (T.C. 2015) (stating that a decision in a CDP hearing without any sort of justification may be an abuse of discretion).<sup>4</sup>

Stark's last argument is about legal fees. His Form 433-A included amounts for *past* legal fees, which were disallowed, but later Stark provided a retainer agreement outlining future costs. The agreement showed a total of \$21,850

<sup>&</sup>lt;sup>3</sup> Part 5.8.5 is different than 5.15.1, where we otherwise look for financial calculations relevant to CNC status. However, the financial analysis for offers in compromise (in part 5.8.5) is similar to that for CNC status, and often cross-references part 5.15.1. We think the logic applies in this situation as well.

<sup>&</sup>lt;sup>4</sup> We also note that in his response to Stark's summary-judgment motion, the Commissioner stated only that there was no factual dispute and rested on the arguments in his initial motion. Had the Commissioner taken the time to reply to this argument, we might not have this problem.

(payable \$500 a month) and included \$4,000 for preparation of a federal offer in compromise, \$2,500 for preparation on a New York offer in compromise, \$600 to evaluate Stark's assets, \$6,500 for other state-tax work, \$750 for investigating the IRS lien, and \$7,500 to defend against potential New York criminal-tax charges. The settlement officer fairly disallowed the amounts for preparing a federal offer and valuing assets because it had already been done, and the amount for criminal charges because none were pending and thus too speculative. But it's unclear what the settlement officer intended to allow. Although she said she'd allow \$16,500, subtracting \$4,000 and \$7,500 (both disallowed amounts) from \$21,850 yields a much smaller amount. And it's unclear from the record how much of the allowable expenses she was allowing per month, which is necessary to determine if a levy would impose a hardship -- the retainer agreement called for \$500 a month to pay off the \$21,850 and perhaps that is what the settlement officer allowed. Also, part of Stark's initial \$497 in claimed legal fees was \$80 a month for related storage. It doesn't appear as if the Commissioner considered this amount, and although it seems as if this might not have been related solely to Stark's legal fees, we can't be sure about the Commissioner's determination on the issue because it isn't explained.

We acknowledge that under abuse-of-discretion review, the Commissioner is given some latitude in his CDP determinations, and we would not find an abuse of discretion if the errors in reasoning and failures to explain were harmless. *See* 5 U.S.C. § 706. But here, where Stark's monthly income looks to have exceeded his expenses by less than \$250, the errors in not increasing his monthly tax expense or allowing for storage and legal fees might well result in a tax levy causing him hardship. Because it was an abuse of discretion not to analyze and decide these questions, we can not sustain the determination to proceed by levy.

When we find an abuse of discretion occurred during a CDP hearing, we generally grant one of two remedies. We either remand the case back to Appeals for a supplemental CDP hearing or deny the collection activity all together. The taxpayer might have a preference as to which remedy we grant. A remand can be helpful if the taxpayer wants a collection alternative and believes a supplementary CDP hearing can produce an agreement with the IRS. Also, a decision not to sustain the determination might not be too fruitful for the taxpayer practically speaking. Our decision only applies to one particular collection action by the IRS and doesn't prevent it from taking subsequent collection actions. In other words, if we don't sustain one levy action, the IRS can propose another one.

There's also potentially a big risk to the taxpayer of not pursuing a remand. I.R.C. § 6320(b)(2) entitles a taxpayer "to only one hearing \* \* \* with respect to the taxable period" corresponding to the notice of lien or levy. It's unclear whether this means the taxpayer isn't entitled to another hearing if the IRS issues a new notice of lien or levy after we don't sustain the first one. Perhaps the taxpayer is entitled to a supplementary hearing on the second notice under the theory it's simply a continuation of the first one. To date, no court has answered this question, and we don't do so here either. We bring it up to highlight the potential risk to the taxpayer.

This isn't to say remand always makes the most sense for a taxpayer. Forestalling a proposed lien or levy may make sense for a taxpayer with ongoing credit problems. For example, our decision not to sustain the determination requires the IRS to withdraw the existing lien and file another one, which could affect its place in line with other creditors of the taxpayer. Also, the timing of filing a notice of lien could have bankruptcy implications. *See*, *e.g.*, 11 U.S.C. § 522(c)(2)(B) ("property exempted under this section is not liable during or after the case for any debt of the debtor that arose \* \* \* before the commencement of the case, except \* \* \* a debt secured by a lien that is \* \* \* a tax lien, notice of which is properly filed"). The advantages or disadvantages of a decision by this Court to not sustain a determination ultimately depend on the peculiar situation of each taxpayer, but there certainly can be instances where the taxpayer prefers this remedy.

Nonetheless, the parties' positions is only one factor we consider in choosing the remedy. Although not determinative, if the parties agree to a remand, we'll generally grant the request. *See, e.g., Moser v. Commissioner*, 104 T.C.M. 98, 99 (2012); *A-Valley Eng'rs, Inc. v. Commissioner*, 104 T.C.M. 69, 70 (2012). But, if the parties don't agree, we'll take the dissenter's objection seriously, though we can still remand the case over the objection. *See Tucker v. Commissioner*, 135 T.C. 114, 118 (2010), *aff'd*, 676 F.3d 1129 (D.C. Cir. 2012). Generally, we find that remand is appropriate when it would be "necessary or productive." *Lunsford v. Commissioner*, 117 T.C. 183, 189 (2001). We look to a number of factors in addition to the preferences of the parties to determine if remand makes sense. Other factors might include:

- the duration of the administrative proceedings to date;
- the length of the pendency of the lawsuit;
- any fault on the part of the party moving for remand;
- whether remand can remedy the defects the first time around, see Wadleigh v. Commissioner, 134 T.C. 280, 299 (2010); Hoyle v. Commissioner, 131 T.C. 197, 204-205 (2008);
- whether remand would be futile because, even though the IRS might've abused its discretion, "the only argument that petitioners presented to this Court were based on legal propositions which we have previously rejected," *Lunsford*, 117 T.C. at 189; and
- whether there has been a material change in the law, *Harrell v. Commissioner*, 86 T.C.M. 378, 383 (2003), or a material change in the facts since the final determination, *Churchill v. Commissioner*, 102 T.C.M. 116, 118-19 (2011).

These are just some factors we'd consider in fashioning the best remedy when the IRS abused its discretion in a CDP hearing. Considering we find the IRS abused its discretion here, we'd like to know where the parties, particularly Mr. Stark, stand on the issue of remanding or not sustaining the determination.

It is therefore

ORDERED that this division of the Court retains jurisdiction. It is also

ORDERED that respondent's summary-judgment motion is denied. It is also

ORDERED that petitioner's summary-judgment motion is granted. It is also

ORDERED that the parties shall file a status report on or before July 29, 2016, stating whether they would prefer a remand or an entry of decision denying collection activity.

(Signed) Mark V. Holmes Judge

Dated: Washington, D.C. June 30, 2016